

Message Text

PAGE 01 TOKYO 09304 110658Z

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ACTION EA-10

INFO OCT-01 ISO-00 SS-15 SP-02 EB-07 INR-07 /042 W

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R 110545Z JUL 75

FM AMEMBASSY TOKYO

TO SECSTATE WASHDC 1506

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EA/J FOR SHERMAN

E.O. 11652: N/A

TAGS: EGEN, PFOR, JA

SUBJ: MIKI VISIT PAPER: JAPAN'S CURRENT ECONOMIC SITUATION

1. JAPAN'S ECONOMY IS ESSENTIALLY STRONG BUT HAS UNDERGONE SEVERE STRAINS OF RAMPANT INFLATION AND MOST SEVERE RECESSION IN POST WAR HISTORY. MAIN POINTS ARE AS FOLLOWS:

2. INFLATION--STILL DOUBLE DIGIT. GOJ HAS SUCCEEDED IN MEETING ITS TARGET TO REDUCE 12 MONTH CPI INCREASE TO BELOW 15 PERCENT (ACTUAL INCREASE: 14.2 PERCENT) FOR FISCAL YEAR ENDING MARCH 31. INCREASE DURING PREVIOUS FISCAL YEAR WAS 24 PERCENT. RATE OF INFLATION DURING APRIL-JUNE APPEARS TO HAVE REMAINED ABOUT 14 PERCENT. GOJ WILL BE HARD-PUT TO MEET ITS GOAL OF HOLDING 12 MONTH CPI INCREASE FOR PERIOD ENDING MARCH 31, 1976 BELOW 10 PERCENT.

3. RECESSION--HAS APPARENTLY TOUCHED BOTTOM. IMPORTANT INDICATORS HAVE TURNED AROUND: UNEMPLOYMENT HAS BEEN DECLINING AND INDUSTRIAL PRODUCTION HAS BEEN INCREASING SLOWLY SINCE FEBRUARY.

4. RECOVERY--WILL BE SLOW. GOJ FORECASE 7 PERCENT ANNUAL REAL GNP GROWTH RATE FOR AUGUST-DECEMBER 1975 (AT OECD ECONOMIC POLICY COMMITTEE JUNE 20) BUT THIS SEEMS A
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PAGE 02 TOKYO 09304 110658Z

BIT TOO HIGH. SUCCESSIVE REDUCTIONS IN THE CENTRAL BANK DISCOUNT RATE (TO 8 PERCENT) HAVE NOT YET PRODUCED VISIBLE RESULTS. ALTHOUGH INVENTORIES HAVE BEEN REDUCED SOMEWHAT, CONSUMER DEMAND IS LAGGING AND MID-YEAR BONUSES

APPEAR TO BE SMALLER THAN USUAL. REAL BUSINESS INVESTMENT FOR 1975 IS EXPECTED TO BE WELL BELOW LAST YEAR, AND GOVERNMENT SPENDING HAS NOT TAKEN UP THE SLACK. TIMING OF RECOVERY IS THEREFORE HIGHLY UNCERTAIN, WITH ESTIMATES OF DEFINITE UPTURN RANGING FROM THIRD QUARTER 1975 TO SECOND QUARTER 1976. UNCERTAINTY SURROUNDING RESUMPTION OF UPSWING CLOUDS PICTURE OVER NEXT 2-3 YEARS, MAKING ACCURATE PROJECTIONS OF REAL GROWTH QUITE DIFFICULT. MOST LIKELY PROSPECT IS FOR ZERO-2 PERCENT REAL GNP GROWTH CY 1975 OVER 1974 FOLLOWED BY 4-6 PERCENT 1976 OVER 1975, ASSUMING: (A) SLUGGISHNESS CONTINUES INTO FALL '75, (B) GOJ ADOPTS MILDLY STIMULATIVE MEASURES WHICH TAKE EFFECT THEREAFTER, AND (C) NO DRASTIC PRICE INCREASE OR INTERRUPTION OF OIL IMPORTS.

5. MEDIUM TERM GROWTH--RETURN TO MIRACLE GROWTH RATES (10-15 PERCENT) IS NOT IN THE PICTURE IF PRESENT POLICIES ARE MAINTAINED, DESPITE SOME UNHAPPINESS IN BUSINESS CIRCLES WITH SLOWER-GROWTH PROJECTIONS. WHEN GROWTH RESUMES IT IS LIKELY TO BE IN 4-6 PERCENT RANGE. CONSTRAINTS MOST OFTEN CITED ARE: NEED TO MODERATE CONSUMPTION OF RAW MATERIALS; DOMESTIC CONCERN ABOUT POLLUTION AND QUALITY OF LIFE; AND LABOR SUPPLY.

6. TRADE--JAPAN, WHICH MUST TRADE TO LIVE, SHARES U.S. COMMITMENT TO OPEN WORLD TRADING SYSTEM AND IS DETERMINED TO WORK FOR SUCCESSFUL CONCLUSION OF CURRENT TOKYO ROUND OF MULTILATERAL TRADE NEGOTIATIONS. DESPITE OVER \$13 BILLION ADDED TO IMPORT BILL BY INCREASED OIL PRICES, JAPAN HAS MAINTAINED TRADE SURPLUS FOR EACH OF 12 MONTHS ENDING MAY '75. RECESSION HAS DAMPENED IMPORTS, INCLUDING THOSE FROM U.S.; U.S. SHARE OF JAPAN'S TOTAL TRADE HAS SLIPPED TO ABOUT 20 PERCENT (FROM 25 PERCENT IN 1973); WE SUPPLIED 21.5 PERCENT OF ITS IMPORTS AND TOOK 19 PERCENT OF ITS EXPORTS IN FIRST FOUR MONTHS OF 1975. JAPAN'S INCREASED EXPORTS (UP 50 PERCENT IN CY 1974 OVER 1973) HAVE LIMITED OFFICIAL USE
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PAGE 03 TOKYO 09304 110658Z

NOT BEEN AIMED AT U.S. FOR FIRST FOUR MONTHS OF 1975 GOJ STATISTICS SHOW 2.5 PERCENT INCREASE IN EXPORTS TO U.S. OVER JAN.-APR. 1974, COMPARED WITH 27 PERCENT INCREASE TO EC AND 28.5 PERCENT INCREASE TO DEVELOPING AREAS. TRADE WITH LDC'S HAS RISEN AS SHARE OF JAPAN'S TOTAL TRADE--IMPORTS TO 54 PERCENT AND EXPORTS TO 48 PERCENT AS OF FIRST QUARTER OF 1975. PROSPECTS ARE FOR JAPAN'S TRADE AND PAYMENTS POSITION TO REMAIN STRONG IN NEAR TERM, WITH YEA MAINTAINING APPROXIMATELY CURRENT STRENGTH VIS-A-VIS DOLLAR.

7. INVESTMENT--OVERSEAS INVESTMENT HAS BEN

LAGGING DUE TO WORLD RECESSION AND SOME TEMPORARY
RESTRAINTS IMPOSED FOR BALANCE-OF-PAYMENTS REASONS;
IT IS EXPECTED TO PICK UP WHEN RECOVERY BEGINS AND
QUADRUPLE (FROM \$10 BILLION TO OVER \$40 BILLION) BY
1980. MUCH WILL BE DIRECTED TO DEVELOPING COUNTRIES.
JAPANESE INVESTMENT IN U.S., CURRENTLY ESTIMATED ABOUT
\$2 BILLION, CAN ALSO BE EXPECTED TO INCREASE SUBSTANTIALLY
IN COMING YEARS. GOJ IS FOLLOWING ITS SCHEDULE FOR
LIBERALIZING RESTICTIONS ON INWARD INVESTMENT. POSSI-
BILITY OF 100 PERCENT FOREIGN OWNERSHIP OF FIRST IN
JAPAN NOW EXISTS IN MOST INDUSTRIES.
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Message Attributes

Automatic Decaptioning: X
Capture Date: 26 AUG 1999
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: ECONOMIC STABILITY, INFLATION, PAPERS, TRADE, MINISTERIAL VISITS, INVESTMENTS
Control Number: n/a
Copy: SINGLE
Draft Date: 11 JUL 1975
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: izenbei0
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1975TOKYO09304
Document Source: ADS
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: n/a
Film Number: D750239-0826
From: TOKYO
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1975/newtext/t197507103/baaaafqw.tel
Line Count: 123
Locator: TEXT ON-LINE, TEXT ON MICROFILM
Office: ACTION EA
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 3
Previous Channel Indicators:
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: n/a
Review Action: RELEASED, APPROVED
Review Authority: izenbei0
Review Comment: n/a
Review Content Flags:
Review Date: 16 JUL 2003
Review Event:
Review Exemptions: n/a
Review History: RELEASED <16 JUL 2003 by BoyleJA>; APPROVED <18 NOV 2003 by izenbei0>
Review Markings:

Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
06 JUL 2006

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: n/a
TAGS: EGEN, PFOR, JA, (MIKI, TAKEO)
To: STATE
Type: TE
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 06 JUL 2006